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C O N F I D E N T I A L SECTION 01 OF 02 MOSCOW 004669

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TAGS: [EPET](#) [ENRG](#) [ECON](#) [PREL](#) [RS](#) [CH](#)

SUBJECT: (C) RUSSIA ENERGY: EXXONMOBIL OPTIMISTIC ON SAKH 1  
GAS DEAL WITH CHINA; GAZPROM SAYS NYET

REF: A. VLADIVOSTOK 102

[1](#)B. MOSCOW 3161

Classified By: Econ MC Eric Schultz for Reasons 1.4 (b/d)

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Summary  
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[1](#)1. (C) ExxonMobil Russia claims to be closing in on a deal to sell China gas from the Sakhalin 1 project it operates. However, Gazprom publicly and privately remains opposed and can block the deal regardless of what ExxonMobil,s contract says. We would not be surprised to see a compromise emerge that both sides can live with. End Summary.

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Deal with China Close  
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[1](#)2. (C) ExxonMobil Russia VP Ed Verona told Econoff August 18 that the company is "very optimistic" it will close a deal with China on gas sales from its Sakhalin 1 project (ref B) despite Chinese foot-dragging. Verona would not speculate on why China is not moving more quickly, but said the company is ready to sign a deal. ExxonMobil remains confident that it has the legal right to sell its gas to whomever it chooses, since its Production Sharing Agreement (PSA) is specifically exempted from the law giving Gazprom an export monopoly. Moreover, its PSA requires the GOR to facilitate the production and sale of Sakhalin 1 oil and gas at the best price available.

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Gazprom Reaction  
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[1](#)3. (C) Verona said he could not predict Gazprom,s reaction to an ExxonMobil-China deal. Gazprom has continued to publicly press ExxonMobil to sell its gas domestically, most recently at the Sakhalin Oil and Gas Conference (ref A). Gazprom has argued that it has the sole legal right to export gas and that the Russian Far East (RFE) needs the gas for its development, something independent energy analysts with whom we,ve talked dispute.

4 (C) Verona reaffirmed that while ExxonMobil is "open to all

commercially competitive offers," it is not/not in negotiations with Gazprom, and does not expect a price offer attractive enough to alter plans to sell to China. "Gazprom seems to believe that if it repeats something often enough in the press, then it becomes true," he said.

15. (C) Ivan Zolotov, Director of External Relations at Gazprom, told Econoff August 20 that ExxonMobil would not be allowed to sell gas directly to China &as long as Gazprom is around.8 He was dismissive of the PSA exclusion.

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Khristenko on the Move?  
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16. (C) Verona expressed some concern about a rumor that Energy Minister Khristenko may leave his post to head Rosneft, which owns 20% of Sakhalin 1. He said that EM is "comfortable" with the current Rosneft leadership and would prefer not to deal with the added uncertainties created by a leadership shuffle.

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Comment  
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17. (C) Sakhalin 1 is the last of the major projects in which foreign companies have a controlling stake (ExxonMobil,s other partners are Japan's SODECO, with 30%, and India's ONGC, with 20%). "Correcting" this "problem" may be on the Kremlin's radar. Furthermore, Gazprom has much at stake in controlling gas prices and terms in dealings with China, potentially its largest future customer, and would not want

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ExxonMobil setting precedents for it in the Chinese market. ExxonMobil appears unwilling to bow to pressure, but we doubt the GOR will allow a deal with China to go forward. We would not be surprised to see a settlement in which half the gas in question goes to Russia,s Far East and half to China, and where Gazprom sells the gas following a deal between ExxonMobil and China on price. End comment.  
Burns